



CITY OF BURBANK
Park, Recreation and Community Services Department
STAFF REPORT

DATE: October 22, 2013

TO: Mark Scott, City Manager

FROM: Judie Wilke, Park, Recreation and Community Services Director

SUBJECT: APPROVAL OF A RESOLUTION APPROVING THE LEASE AND OPERATING AGREEMENT BETWEEN THE CITY OF BURBANK AND S.S. GOLF, INC. FOR THE DEBELL GOLF COURSE AND THE RELATED EXEMPTION FROM THE CALIFORNIA ENVIRONMENTAL QUALITY ACT

RECOMMENDATION

Staff is requesting three actions from the City Council:

- 1) Adopt a resolution approving the Lease and Operating Agreement between the City and S.S. Golf, Inc. (S.S. Golf) to manage the ongoing operations of the DeBell Golf Course, as well as the related exemption from the California Environmental Quality Act (Exhibit A);
- 2) Amend the DeBell Golf Fund (Fund) Fiscal Year (FY) 2013-2014 cost allocation figure by \$94,500 to more appropriately reflect the new operation structure of the Fund; and,
- 3) Postpone existing capital improvement projects and direct staff to prepare a realistic capital improvement plan to complete these projects.

BACKGROUND

The Golf Fund is an Enterprise Fund and pursuant to the City's Financial Policies, the Fund must cover all maintenance, operational and capital improvement costs of the DeBell Golf Course and Clubhouse. However, in March 2011, the City Council (Council) was informed that the Fund was not meeting the City's Financial Policies and had depleted its cash balance.

Prior to the construction of the Clubhouse, the Fund had over \$6 million in reserves; however, a number of factors lead to the Fund's structural deficit including: 1) reserve funds were fully exhausted to construct the Clubhouse and the General Fund had to make a loan to the Fund to complete the project; 2) the depletion of all reserve funds impacted the Fund's ability to realize any accumulated annual interest earnings; 3) operating costs increased over the last five years; and 4) a nationwide economic

downturn in the game of golf significantly impacted participation or rounds of golf played at the DeBell Golf Course.

With the Fund seriously compromised, the Council and staff began to systematically address various financial and operational aspects to improve both the Fund's existing structural deficit and ongoing operations.

- The first action the Council took was on June 7, 2011. The Council approved a \$1 million loan from the General Fund to immediately improve the Fund's operating deficit.
- Then on July 12, 2011, the Council established the Golf Fund Oversight Committee to provide heightened oversight of the Fund and make recommendations to the Council on matters related to the operations of the Golf Course.
- On September 20, 2011, the Council approved an agreement with National Golf Foundation (NGF) to conduct a comprehensive independent review and assessment of the DeBell Golf operations.
- On February 23, 2012, NGF presented the Council with a formal report summarizing their assessment of the DeBell Golf Course and Clubhouse operations and recommendations to improve the financial and operational condition of the DeBell Golf Course and Fund. In summary NGF's recommendations were as follows: 1) pursue a full-service management contract; 2) develop a comprehensive long range plan for capital projects; 3) consider a plan to reduce the direct administrative responsibility for DeBell Golf Course, thus reduce City overhead charged to the Fund; 4) improve marketing efforts for the facility; 5) improve the cohesiveness of services provided by each of the operations; and 6) align greens fees with similar courses within the area (Exhibit B).

In conformance with these recommendations, on October 25, 2012, the Council and the Park, Recreation and Community Services (PRCS) Board held a joint meeting to discuss the future management structure of the golf course operations. Following an extensive discussion, the Council and Board agreed that the best course of action was to proceed with a full-service management contract as recommended by NGF. It was determined that this structure would attain the goal of removing the City from the day-to-day responsibility of managing DeBell, which would significantly reduce the City's overhead and involvement. The Council and PRCS Board also believed that the single operator structure would ensure a more coherent and cohesive operation, minimizing conflicts that may arise between competing interests.

Pursuant to the Council direction and consistent with the PRCS Board's recommendation of developing a full-service management contract with the current operators, staff began working with the existing operators to develop an agreement. On December 4, 2012, R&M Concessions, Inc. (food and beverage concessionaires) advised staff that they were no longer interested in working towards this full service structure and would instead operate the Clubhouse in accordance with their existing agreement through its expiration on December 31, 2013.

On January 10, 2013, staff provided the PRCS Board and subsequently on February 5, 2013 the Council with an update on the development of this full service management structure. In alignment with the discussions that took place at the joint meeting, the Council unanimously recommended that staff continue working with Mr. Scozzola, the president of S.S. Golf knowing that a new food and beverage operator would need to be selected.

DISCUSSION

With direction provided by both the Board and Council, staff continued working with S.S. Golf to negotiate a full-service management agreement and on April 29, 2013 S.S. Golf provided staff with their formal proposal. The terms of S.S. Golf's proposal have been reviewed by the City Attorney's Office, City Manager and Financial Services Director. The agreement before the Council was drafted by staff and the City Attorney's Office and negotiated with S.S. Golf (Exhibit C). The main deal points have been summarized in Exhibit D; however, following is a summary of the main components of the agreement.

As a full-service management agreement, the DeBell Golf Course and its associated facilities will be leased to S.S. Golf for a fixed term (five and a half years) and for a minimum price (\$300,000 annually). Mr. Scozzola will be responsible for the day-to-day operations and management of the entire facility which includes, but is not limited to the following: the promotion and management of the golf course and restaurant operations, the hiring of all employees, the negotiation of all operations and maintenance service contracts, the development of a long range capital improvement program, the collection and disbursement of all monies, and the purchase and maintenance of all licenses and insurances for the entire facility.

Given the terms of this agreement, S.S. Golf will lease all the assets associated with the operations of the DeBell Golf Course in an as-is condition for the term of the agreement. This includes both golf and restaurant related equipment and fixtures. S.S. Golf will be required to perform ongoing maintenance and will be responsible for the replacement of any equipment. Even though the City purchased the kitchen equipment and restaurant fixtures as part of the Clubhouse project (estimated initially at \$380,000) the value and useful life of the equipment has depreciated over time. An assessment to determine the value and useful life of the existing kitchen equipment was completed. Per the assessment, the kitchen equipment could sell on the open market for approximately \$35,000 - \$40,000. Rather than requiring S.S. Golf to purchase the equipment, staff believes the more viable option is to have S.S. Golf take the kitchen equipment in an as-is condition and be responsible for its on-going maintenance and replacement.

To accomplish the City's goal of having a full service management operation, S.S. Golf has formed a strategic relationship with Valley Crest for grounds maintenance and with Mr. Tom Shayman, owner and operator of Burbank Bar and Grill, for restaurant operations. Mr. Scozzola will serve as the main point of contact and all other operations, though separate entities, will be under the operational umbrella of S.S. Golf.

The focus of this new arrangement will create a synergistic relationship of operations that will enhance the overall golf experience at DeBell Golf Course. Valley Crest will continue to be responsible for maintaining the golf course and associated landscapes; while Mr. Shayman will be responsible for the daily operations of the restaurant, which will be rebranded as the Canyon Grill. Mr. Scozzola will not only be responsible for managing and overseeing the operations of the course maintenance and restaurant operations, but he will also be responsible for securing other incidental services such as janitorial and golf cart maintenance, to adequately serve the public using the facility.

Staff believes that this agreement will achieve the best operational structure by supporting a strong partnership with S.S. Golf that will:

- Minimize the City's day-to-day involvement in the operation, thereby allowing the operator to be in a position to address matters at DeBell in a more expeditious and effective way.
- Require the operator to meet the City's established program requirements, ensuring that DeBell remains focused on the community it serves with respect to the budget, fees, operations, maintenance and programming.
- Simplify the current revenue sharing structure to ensure the City can meet its debt payments, financial obligations, and eventually set aside some funding towards ongoing capital needs.
- Share the risk with the operator, while allowing the City to maintain some control in the operations.

The negotiated agreement was reviewed by NGF and the PRCS Board. Staff believed it was important to have NGF conduct an independent review of the agreement to ascertain whether it appropriately reflected the operations of the DeBell Golf Course and was in line with other similar courses operating under a full service management structure. In summary, NGF agreed that the proposed agreement addressed many of the concerns presented in the analysis that was completed in 2011 (Exhibit E). NGF also noted that the proposed agreement was reasonable and fairly represented both the City's and S.S. Golf's interests.

The PRCS Board reviewed the terms of the proposed agreement at its August and September meetings. The PRCS Board's recommended changes were incorporated into the agreement and on September 12, 2013, they unanimously recommended approval of the proposed agreement to the Council.

The lease is categorically exempt from the California Environmental Quality Act ("CEQA") in accordance with Section 15301 of the CEQA Guidelines pertaining to leasing public or private structures involving negligible or no expansion of use beyond that which already exists.

FISCAL IMPACT

As part of this agreement, the City is guaranteed to receive a base rent of \$300,000 annually. Burbank Municipal Code Section 2-2-201 authorizes a private lease for City property, when such lease is not less than fair rental value as determined by appraisal.

A letter of appraisal by NGF determined the fair rental value to be between \$290,000 and 330,000 (Exhibit F). Therefore, the base rent as proposed falls within this range.

The base rent payments will be used to cover existing annual loan obligations of \$128,704 (\$78,704 for the first loan and \$50,000 for the second loan). As a reminder, on March 7, 2006 and subsequently on June 17, 2007, the Council approved a loan in the amount of \$2.9 million from the General Fund to finance the construction of the Clubhouse. The Council approved an additional loan on June 7, 2011 in the amount of \$1 million from the General Fund to improve the Fund's operating deficit. To address the Fund's continued financial position, on April 23, 2013 the Council amended the terms of both loans by deferring the repayment of the first loan to January 1, 2019 and the second loan until January 1, 2016.

Additionally, base rent payments will be used to cover direct and allocated costs related to administering the contract. Should the terms of the agreement be approved, the new management structure will require less direct City involvement and staff oversight. Therefore, the Fund will realize a significant savings in the reduction of City overhead. Due to the new management structure, staff anticipates that the City's cost allocation figure may be reduced from its current figure of \$348,984 to approximately \$160,000.

Given that the agreement will commence on January 1, 2014, staff recommends that the Council consider amending the Fund's FY 2013-2014 cost allocation and reduce a portion of the Fund's remaining payments for FY 2013-2014 (\$174,492; January - June) by \$94,500 to reflect the new management structure. It is the City's Financial Policy to allocate costs in accordance with time that was spent in the prior year; however, staff believes that because the Fund will be operating under a new business model in January, the Fund's FY 2013-2014 cost allocation figure should be adjusted accordingly. It would not be appropriate to charge the Fund for higher levels of overhead no longer being provided. Staff believes that there will be a 40%-60% reduction in the amount of time allocated towards overseeing this Fund. While this is a reasonable approach for the Fund, it is important to note that this action will negatively impact the General Fund because cost allocation is a major revenue source that has been incorporated into the City's annual budget. Therefore, approving this action will result in a \$94,500 revenue reduction to the General Fund.

Finally, base rent payments will also be used to cover any ongoing major facility maintenance costs associated with the Clubhouse. As a City facility, the City will be responsible for performing and completing any major maintenance to the Clubhouse which includes plumbing, electrical, roofing, painting, etc. The distinction between major and minor maintenance has been negotiated with S.S. Golf and are included in the agreement.

The agreement also has a provision in which additional rent payments will be made. Should total gross revenues exceed a certain threshold (\$2,499,999) S.S. Golf will provide the City with an additional payment at a higher percentage. This additional rent payment is calculated based on the difference between the base total gross revenue of \$2,499,999 and the realized total gross revenue. It is anticipated that the percentage rent payment could range from \$20,000 to \$30,000 in year one and increase to \$25,000

to \$35,000 in year two. The City intends to use these payments as a means to accelerate existing loan obligation payments and to help supplement any capital improvement contributions that S.S. Golf provides, as required per the approval of this agreement.

The agreement has a provision in which S.S. Golf is required to make annual contributions towards a Capital Improvement Fund which is based on 0.75% of total gross revenues. It is anticipated that in the second year, when this provision commences, S.S. Golf will provide the City with a capital improvement contribution that could range from \$15,000 to \$30,000. Contributions will be used to fund any future capital expenditures both course and restaurant related. It is anticipated that capital improvement expenses will not commence until the fourth or fifth year when there will be ample reserves accumulated to fund projects. Furthermore, as part of this agreement, S.S. Golf will have to prepare and submit annually to the City a five year capital plan which will be used to collectively determine how best to allocate these funds. While this is not a significant capital improvement program, it is a start towards building one. Currently, the Fund is not setting aside any funding to cover any future capital improvement projects.

S.S. Golf's capital contributions will not be used to cover any existing capital improvement projects which include the following: cart path improvements (est. \$80,000) and seismic retrofit of several auxiliary buildings and demolition of three buildings on the golf course (est. \$350,000). These projects will be completed pending the Fund's available cash balance. At this point there is no cash available so staff will prepare a realistic plan to address these existing and needed capital projects over the next three to five years.

Based on all these assumptions, staff anticipates that the Fund will receive \$320,000 to \$330,000 in the first full year of operation (2014-15) and \$350,000 to \$365,000 in the second year.

Fund Cash Flow:

Actions previously taken by the Council have significantly improved the Fund's financial position. More importantly, the Fund's FY 2012-2013 year-end cash balance remained the same as FY 2011-2012 which is an indicator that the Fund is improving but certainly not at the point where it has significant cash reserves to complete any capital projects (Exhibit G).

The main reason the cash position of the Fund has neutralized is because major capital improvement projects have been postponed, expenditures were reduced and revenues have been consistent over the past couple of years. Though the cash position of the Fund has stabilized, the Fund still does not have the necessary revenue stream to support existing and future capital costs or depreciation. It is also important to note that although the terms of the agreement should allow the City to operate the Fund on a cash positive basis, similar to the current situation, the Fund will still be unable to cover the depreciation of the facilities.

Should both the terms of this agreement and the recommendations as outlined in this report be approved (forgiving a portion of the Fund's cost allocation and postponing capital improvement projects), the Fund's financial position is projected to significantly improve. Staff is projecting the Fund's FY 2013-2014 year-end cash balance to be \$98,000.

During the agreement's first full year of operations, the Fund's FY 2014-2015 year-end cash balance is projected to be \$197,000. This is a forecast that the terms as proposed will positively impact the financial position of the Fund. Furthermore, Years 3 through 5 of the agreement not only produce a gradual increase in the Fund's year-end cash balance, but there is also a sufficient amount of funding to begin repaying existing loan obligations.

While this new management arrangement will move the Fund toward a better financial and operational direction, the reality is that the Fund will not earn enough income to address the current and future capital project needs. For a number of years the Fund has needed to accomplish a variety of capital projects including irrigation improvements, tee box renovations, golf cart path improvements and driving range improvements. However, all have been put off because there are no available funds to complete them. The only projects undertaken in the past five years were minor irrigation improvements along hole number five and the commencement of design work for golf cart improvements.

The entire course and clubhouse are community assets that need to be properly maintained. In addition, there are possible capital projects that could potentially increase revenue (i.e. covered driving range, enhanced cart paths). While it is great news that this Agreement for the first time creates a mechanism whereby funds will be set aside by the operator for capital projects, the projected amount will not generate nearly enough cash to properly maintain/improve the course until 2022, if then.

Realistically, the Fund will not be able to sustain its current condition without forgoing capital projects. While the City can continue putting the capital projects off, that will only be feasible for possibly another 3 to 5 years. In addition to the seismic retrofit project that needs to be completed, there is deferred maintenance on the tees, cart paths, irrigation, etc., that have to be addressed or the ultimate fix may be more costly. Therefore, at some point, the City is going to have to consider ways to meet the capital demands. Unless other fundamental assumptions change, it is likely the General Fund will have to further assist the Fund. In this regard, there are a number of options:

1. The City could consider forgiving one or both of the loan payments;
2. Use General Fund dollars to pay for immediate needed capital projects; or,
3. Subsidize programs at the golf course (i.e. youth programs) that meet with the Councils stated goals.

Between what the operator is paying and what the City could contribute, the Fund should eventually be able to accrue \$100,000 annually to spend on necessary maintenance and desired improvements. Thus, it is the current (backlogged) capital projects that are impossible for the Fund to address without assistance from the

General Fund. However, once those projects are completed, there should be adequate funding to prepare a strategic capital improvement program that keeps the golf course and clubhouse in good condition.

CONCLUSION

In alignment with the PRCS Board's recommendation and Council direction, staff believes that the Agreement will achieve the best operational structure by not only supporting a strong partnership between the City and S.S. Golf but it will also ensure that the DeBell Golf Course and Clubhouse is appropriately maintained and operated for future generations to enjoy. In summary, staff recommends that the Council consider the following:

- 1) Adopt a resolution approving the Lease and Operating Agreement between the City and S.S. Golf to manage the ongoing operations of the DeBell Golf Course, as well as the related exemption from the California Environmental Quality Act;
- 2) Amend the Fund's FY 2013-2014 cost allocation figure by \$94,500 to more appropriately reflect the new operational structure of the Fund; and,
- 3) Postpone existing capital improvement projects and direct staff to prepare a realistic capital improvement plan to complete these projects.

LIST OF EXHIBITS

Exhibit A:	Resolution
Exhibit B:	National Golf Foundation Recommendations
Exhibit C:	Lease and Operations Agreement
Exhibit D:	Summary of Agreement Deal Points
Exhibit E:	Comments Provided by NGF's Related to Review of Proposed Agreement
Exhibit F:	NGF Fair Market Rent Letter
Exhibit G:	Revised Cash Flow